Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

Competitive Telecommunications Association, Florida Competitive Carriers Association, and Southeastern Competitive Carriers Association	)	
	)	CC Docket No. 98-99
Petition On Defining Certain Incumbent LEC Affiliates As Successors, Assigns, or Comparable Carriers Under Section 251(h) of the Communications Act	)	

REPLY COMMENTS OF MCI TELECOMMUNICATIONS CORPORATION

MCI TELECOMMUNICATIONS CORPORATION

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SUMMARY

Because the ILECs' local service affiliates are not intended to compete with the ILECs, such affiliates are the antithesis of CLECs, and must be treated in every way like ILECs. Unless the Commission rules that, under Section 251(h), an ILEC-affiliated local service provider can be subject to the Section 251(c) obligations of ILECs, ILEC local service affiliates will facilitate ILECs' avoidance of their Section 251 obligations.

Contrary to the ILECs' contentions, there are no procedural obstacles in the way of an interpretive declaration outlining the conditions under which an ILEC local service affiliate might be deemed a successor or assign of the ILEC under Section 251(h)(1). The ILECs mischaracterize the Non-Accounting Safeguards Order as having concluded that transfer of ownership of network elements by an ILEC to an affiliate is the only way the affiliate could be deemed a successor or assign of the ILEC. It is still an open question as to what other circumstances might also result in such a status for the affiliate. That order also left open the issue of what circumstances would justify such an affiliate being deemed a comparable carrier under Section 251(h)(2).

As to the merits of the CompTel Petition, the ILECs have failed to explain why an ILEC affiliate providing local service could not be deemed an ILEC under any circumstances. The cases they cite construing the meaning of "successor" or "assign" must be read together with cases supporting the proposition that the corporate form of organization must be ignored where necessary to

fulfill statutory goals. Thus, the Commission should apply the terms of Section 251(h) so as to effectuate the local competition goals of Section 251.

Some ILECs argue that an ILEC could not use its affiliate to evade its Section 251(c) obligations if the affiliate itself is obtaining UNEs and services from the ILEC that must be offered to all others at the same rates, terms and conditions. But such an evasion has already occurred, with the Connecticut DPUC authorization of the SNET reorganization plan, which resulted in the removal of the resale requirement in Section 251(c)(4) from SNET's local services.

The SNET example shows that if an ILEC affiliate is providing local services that the ILEC does not provide at retail, the resale requirements of Section 251(c)(4) can be avoided, since the affiliate's unique services offerings will not be available for resale at a wholesale discount. In the absence of such a discount, it hardly matters that the affiliate does not legally own any bottleneck facilities, since it can carry out these anticompetitive strategies using the ILEC's bottleneck facilities, while incurring none of the obligations normally attending the use of such facilities.

An ILEC affiliate operating in tandem with the ILEC clearly occupies a dominant position that enables it to make competitive entry more difficult unless it is subject to the obligations of Section 251(c). Therefore the affiliate should be treated like an ILEC under Section 251(h) and should be treated as dominant.

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Competitive Telecommunications Association, Florida Competitive Carriers Association, and Southeastern Competitive Carriers Association	)	
Petition On Defining Certain Incumbent LEC Affiliates As Successors, Assigns, or Comparable Carriers Under Section 251(h) of the Communications Act	)	CC Docket No. 98-39

REPLY COMMENTS OF MCI TELECOMMUNICATIONS CORPORATION

MCI Telecommunications Corporation (MCI), by its undersigned attorneys, hereby replies to the initial comments on the above-captioned Petition for Declaratory Ruling or, in the Alternative, for Rulemaking filed by the Competitive Telecommunications Association, et al. (CompTel Petition).[1] Although the comments filed by the Bell Operating Companies (BOCs) and other incumbent local exchange carriers (ILECs) purport to address the legal and regulatory issues raised by the CompTel Petition, they do so in a vacuum, with no reference to the actual factual context in which those issues must be analyzed.

Those comments thus fail to come to grips with the reality, as explained in MCI's and other competitive carriers' comments, that the ILECs' local service affiliates are not intended to compete with the ILECs, but, rather, to coordinate their operations closely with the ILECs. Such affiliates thus are the antithesis of competitive local exchange carriers (CLECs) and

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[1] Commission Seeks Comment on Petition Regarding Regulatory Treatment of Affiliates of ILECs, CC Docket No. 98-39 DA 98-627 (released April 1, 1998).

must be treated in every way like ILECs, so as not to undermine the goals of Section 251.

A. Introduction

The ILECs all present variations on the argument that the interpretations of Section 251(h) sought by CompTel et al. are directly contrary to the recognized meaning of the terms of that provision and thus cannot even be considered, whatever the facts may be. Thus, they assert that, where an ILEC will continue to exist in its current form, its affiliate providing wireline local exchange or exchange access service within the ILEC's service region cannot be considered, in the absence of a transfer of assets or network capabilities, a "successor or assign" of the ILEC under Section 251(h)(1)(B)(ii) of the Communications Act. Similarly, they claim that such an affiliate cannot possibly, under any circumstances, be considered a "comparable" carrier to the ILEC under Section 251(h)(2). They also dispute that the affiliate should be subject to the obligations of ILECs under Section 251(c) or be treated as a "dominant carrier" for the provision of interstate services.

Some of the ILECs also argue, in one form or another, that CompTel's request has already been denied in whole or in part in the Non-Accounting Safeguards Order[2] and that the CompTel

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[2] Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as Amended, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21905 (1996), recon. pending (subsequent history omitted).

Petition is therefore an untimely petition for reconsideration of that order. They also argue that since that order is subject to pending reconsideration petitions, no rulemaking or declaratory relief affecting the same issues can be considered at this time.

B. There Are No Procedural Obstacles to the Relief Sought by CompTel, et al.

Taking the latter issue first, the ILECs' procedural objections are incorrect on several grounds. First, as CompTel et al. point out, the Non-Accounting Safeguards Order did not directly address the precise issues raised in this proceeding. That order held, in relevant part:

> 1. If a BOC transfers to an affiliate ownership of any network elements that must be provided on an unbundled basis pursuant to Section 251(c)(3), such entity will be deemed an "assign" of the BOC with respect to those elements.[3]
>
> 2. A BOC affiliate should not be deemed an ILEC, or, more specifically, a "comparable" carrier under Section 251(h)(2), "solely" because it offers local exchange services.[4]

As to the first point, there is no suggestion in the Non-Accounting Safeguards Order that a BOC affiliate could not become a successor or assign of the BOC in any number of other ways, in addition to a transfer of ownership of network elements. In fact, such a transfer is presented simply as an "example" of the ways in which a BOC might try to evade the Section 251

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[3] Id. at ¶ 309.

[4] Id. at ¶ 312.

requirements.[5] That order certainly does not say, or even imply, that such a transfer is the only way that a BOC affiliate might become a successor or assign of the BOC, and the ILECs' mischaracterizations of that order as having concluded that such a transfer is the "only" way that an affiliate could be deemed a successor or assign must be rejected.[6] Thus, there is nothing standing in the way of an interpretive declaration outlining the conditions under which an ILEC affiliate might be deemed an ILEC under Section 251(h)(1).

Similarly, there is also nothing in that order to the effect that a BOC affiliate providing local service could not be considered a comparable carrier or otherwise deemed an ILEC under any set of circumstances. It simply concludes, based on the record before it, that ILEC status cannot be based "solely" on the affiliate's provision of local service.

Moreover, to the extent that related issues were resolved in the Non-Accounting Safeguards Order, there is no procedural obstacle to the initiation of a new rulemaking or declaratory ruling proceeding to review those issues along with the issues raised in the CompTel Petition based on a new record. By definition, such procedures assume the legal finality of the current regulatory regime and seek to change or interpret some aspect of it. Ameritech argues that the relief CompTel seeks is

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[5] Id. at ¶ 309.

[6] See, e.g., Bell Atlantic Comments at 4; Ameritech Opposition at 4; SNET Comments at 6; BellSouth Comments at 15.

inconsistent with the Non-Accounting Safeguards Order and thus requires "a rule change."[7] That is what a rulemaking proceeding does; it brings about a change in the rules.

BellSouth asserts that CompTel et al. did not seek reconsideration of the Non-Accounting Safeguards Order on the issue of the provision of local service by Section 272 affiliates and that this is an untimely petition for such reconsideration.[8] As explained above, the CompTel Petition does not raise the issues that were actually decided in that order, but it should be noted, in any event, that MCI did challenge, in its petition for reconsideration of the Non-Accounting Safeguards Order, the decision to allow the BOCs' Section 272 affiliates to provide local services, based on some of the same policy reasons that MCI and other parties have raised in support of the CompTel Petition.[9] It would be more efficient, in terms of administrative resources, to consider that issue in the context of the CompTel Petition, since the CompTel Petition raises the broader question of the appropriate legal and regulatory status of any ILEC affiliate providing local service under certain circumstances, rather than just the provision of local services

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[7] Ameritech Opposition at 8.

[8] BellSouth Comments at 3, 6.

[9] See Petition for Reconsideration of MCI Telecommunications Corporation, CC Docket No. 96-149 (filed Feb. 20, 1997).

by the BOCs' Section 272 affiliates.[10] Accordingly, there are no procedural obstacles to a consideration of the CompTel Petition at this time.

C. The ILECs Fail to Take Into Account the Applicable Legal Principles or a Realistic View of the Facts

On the merits, the ILECs have failed to explain why an ILEC affiliate providing local service could not be deemed an ILEC under any circumstances. First, their discussions of case law do not support their implicit argument that the circumstances should always be ignored in applying Section 251(h). The cases they cite construing the meaning of "successor" or "assign," as well as the other legal principles they cite, must be read together with cases supporting the proposition that the corporate form of organization must be ignored where necessary to fulfill statutory goals.

As the court held in General Telephone Co. v. United States, 449 F.2d 846 (5th Cir. 1971), in upholding the Commission's authority to require non-carrier affiliates of common carriers to obtain Section 214 certification in order to construct CATV channel services,

> the activities of the non-common carrier affiliates [in that situation] may be imputed to the common carrier parent.... Where the statutory purpose could ... be easily frustrated through the use of separate corporate

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[10] To the extent that there is an overlap between the policy arguments relevant to the reconsideration issues and the CompTel Petition, consideration of both sets of issues in tandem will allow the Commission to take account of the broadest possible record in fashioning effective relief.

> entities, the Commission is entitled to look through corporate form and treat the separate entities as one and the same for purposes of regulation.

Id. at 855. Similarly, in Transcontinental Gas Pipe Line Corp. v. FERC, 998 F.2d 1313, 1321 (5th Cir. 1993), the court held, citing General Telephone, that where a natural gas supplier set up two subsidiaries to sell gas at prices at which it could not legally sell, all three could be treated as one entity for purposes of applying the gas price regulations. Here, the Commission should apply the terms of Section 251(h) so as to effectuate the purposes of Section 251, even if that requires that the Commission "look through corporate form."

Second, although, in some instances, the ILECs appear to recognize similar principles, they take an unrealistic view of the factual context in which those principles should be applied. For example, Ameritech correctly states that "whether or not an ILEC affiliate is an ILEC assign is a determination that must be made with reference to the specific purposes of section 251(c)."[11] BellSouth also correctly observes that "the regulatory status of an affiliate is determined by the functions and capabilities it possesses, not simply its afiliation."[12] The ILECs, however, take a crabbed view of the purposes of Section 251 and the potential functions and capabilities of ILEC local service affiliates, thereby misapplying their stated principles.

Thus, some of the ILECs argue that an ILEC could not use its

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[11] Ameritech Opposition at 16.

[12] BellSouth Comments at 4.

affiliate to evade its Section 251(c) obligations if the affiliate itself is obtaining unbundled network elements (UNEs) and resold services from the ILEC, which must offer the same UNEs and services to all.[13] Ameritech also claims that ILECs cannot transfer their customers to unregulated affiliates, since that would constitute "slamming."[14]

As CompTel et al., MCI and others have explained, however, these violations have already occurred. The Connecticut Department of Public Utility Control (DPUC) authorized precisely such an end run around Section 251(c)(4) in approving Southern New England Telephone Company's (SNET's) reorganization plan. In granting such approval, the DPUC upheld one of the avowed purposes of the plan, which was to avoid SNET's Section 251(c)(4) obligation.[15] Because SNET America Inc. (SAI) would inherit SNET's retail operations and customers and would provide all retail services in SNET's place, the DPUC concluded that the resale duties of Section 251(c)(4) would no longer apply to SNET, while Section 251 would not be applicable at all to SAI, since it

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[13] See, e.g., Ameritech Opposition at 17.

[14] Id.

[15] See Decision at 13, DPUC Investigation of the Southern New England Telephone Company Affiliate Matters Associated with the Implementation of the Public Act 94-83, Docket No. 94-10-05 (Conn. DPUC June 25, 1997)(SNET "contends that the most notable market disadvantage presented to the [SNET] Telco is the requirement that it provide, at wholesale, essentially all of its retail telecommunications services including discount plans, service packages and promotions, at a [discount calculated pursuant to the 1996 Act]").

is not an ILEC.[16] Thus, competitors are deprived of the opportunity to purchase at wholesale the service packages and promotions that are offered by SAI but not by SNET, thereby removing an important competitive safeguard on SNET/SAI's behavior. Moreover, SNET's customers are all being transferred to SAI.

In view of this history, it is ironic that SNET and other ILECs cite the SNET reorganization plan as precedent for their reading of what is a successor or assign of an ILEC.[17] SNET regards the DPUC approach as "instructive." It certainly is, although not for the reason SNET suggests, but, rather, because it demonstrates the need for Commission action in this area to enforce Section 251.[18] It is precisely that type of deliberate avoidance of the Section 251 obligations that requires an interpretation of "successor" or "assign" that fulfills, rather than frustrates, the purposes of Section 251. Similarly, BellSouth's reference to the state commissions that have granted ILEC local service affiliate certifications[19] is simply a further demonstration that Commission action is necessary. Thus, unless the Commission "look[s] through corporate form ... for purposes of" applying Section 251(h), "the statutory purpose [of Section

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[16] Id. at 52-54.

[17] See SNET Comments at 9, n.9; Ameritech Opposition at 12-13.

[18] SNET Comments at 9, n.9.

[19] BellSouth Comments at 7-8.

251] could ... be easily frustrated through the use of separate corporate entities."[20]

As if to drive CompTel's point home, Ameritech cites the position of the Department of Justice that the spin-off of AirTouch from Pacific Telesis was an example of a true successor or assign of Pacific.[21] In fact, however, AirTouch is only the successor of Pacific as to its cellular business, just as an ILEC local service affiliate should be deemed the successor or assign of the ILEC as to those customers who migrate to the affiliate, particularly for services and features not available from the ILEC.

Similarly, Sprint reports that Ameritech is using a local service affiliate in one of its states to provide xDSL services that the Ameritech ILECs do not offer. This is the same type of evasion of Section 251 obligations that the BOC petitions for relief under Section 706 were intended to achieve.[22] If an ILEC affiliate is providing local services that the ILEC does not provide at retail, the resale requirements of Section 251(c) can be evaded, since the affiliate's unique service offerings will not be available for resale at a wholesale discount. In the absence of such a discount, it hardly matters that the affiliate does not legally own any bottleneck facilities, since it can carry out these anticompetitive strategies using the ILEC's

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[20] General Telephone, 449 F.2d at 855.

[21] Ameritech Opposition at 13.

[22] Sprint Comments at 4.

bottleneck facilities, while incurring none of the obligations normally attending the use of bottleneck facilities. Favored large customers can be migrated to the affiliate through the offering of services that the ILEC has ceased to offer or through the offering of special features and service bundles not available from the ILEC, at rates, terms and conditions not available from the ILEC. GTE virtually promises in its comments to make such offers.[23]

That the ILEC UNEs and "piece-part" services used by the affiliate are also theoretically available to others at the same rates, terms and conditions[24] does not make up for the unavailability of the affiliate's unique retail services at a wholesale discount.[25] Since the affiliate, which coordinates with the ILEC, can be used to "pick off" incipient competition by targeting particular offerings to large customers, the ILEC will still benefit on a corporate-wide basis even though such offerings are not profitable to the affiliate, considered separately, in light of its imputed costs. Other CLECs thus will not be able to offer a competing service at a competitive rate using the underlying services available at tariffed rates from the ILEC. In these circumstances, the affiliate, in tandem with the ILEC, "performs the functions of an ILEC," to use BellSouth's

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[23] GTE Comments at 3.

[24] See, e.g., Frontier Comments at 5.

[25] See BellSouth Comments at 14 (ILEC local service affiliate would not offer its services at wholesale discount).

formulation of the standard that should be applied,[26] and the affiliate therefore should be treated like an ILEC.

It is also no protection that, as BellSouth argues, if the ILEC affiliate sells local service below its cost, other CLECs could buy such services and resell them, and the ILEC affiliate would lose money on such sales.[27] Whether or not the affiliate, considered separately, loses money is irrelevant. As long as the ILEC makes a profit on a corporate-wide basis, the service is profitable. Furthermore, that other CLECs are able to purchase the affiliate's underpriced services will not do them any good, since they still will not be able to compete with services offered by the affiliate at a loss. Finally, even company-wide losses can be useful if they chill incipient competition. As discussed above, the affiliate would only be targeting such offers to those large customers who would be most likely to seek offers from other CLECs, thereby foreclosing such competition before it gets started. Such offers could also be "fenced," so that other CLECs could not take advantage of them, even though they were nominally available to all similarly situated customers on a nondiscriminatory basis.

It should be noted, in connection with the customer migration strategies discussed above, that Ameritech's comment about "slamming" is ludicrous. Obviously, the migration of customers that accompanies the market division strategies

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[26] Id. at 5.

[27] Id. at 7.

discussed above does not have to be forcible, as it was in the case of the SNET reorganization. Typically, the affiliate would be providing favored large customers with features and service bundles not available from the ILEC, which would draw those customers away from the ILEC. The affiliate's local services also would not be available for resale at a discount, nor would its access services necessarily be available to all at the same rates, terms and conditions, if it were treated as nondominant.

Perhaps the ILECs' most egregious flight from reality is their unsupported and unbelievable contention that ILEC local service affiliates will be competing with their affiliated ILECs. BellSouth, for example, claims that its local service affiliate, BSE, will compete with its incumbent operating affiliate, BST, and that they will not share customers.[28] SBC also asserts that such affiliates will compete with the ILECs.[29] As MCI pointed out in its initial comments, however, BellSouth has already testified to the contrary, and various state commissions have expressed doubts that such affiliates would ever actually compete with their own ILECs.[30] It would be unrealistic for the Commission to assume such competition, since it would undermine the ILECs' whole purpose in establishing such affiliates.

Some of the ILECs also make a point of the fact that their brand name, trademark and logo are owned by the corporate parent,

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[28] Id. at 18.

[29] SBC Comments at 9.

[30] MCI Comments at 6-9 & n. 5.

not the incumbent local operating company, and that the parent, rather than the operating company, is the source of capital.[31] The real issue, though, is whether resources are being utilized in a way that evades the purposes of Section 251. If the parent is providing resources that enable its wholly-owned operating companies to evade Section 251, "the Commission is entitled to look through corporate form" so as not to "frustrate[]" the "statutory purpose" of Section 251.

Some of the ILECs cite the Guam NPRM[32] as demonstrating that an affiliate providing local service in the ILEC's service territory would not constitute a comparable carrier under Section 251(h)(2). In the Guam NPRM, however, the Commission tentatively rejected "an overly literal reading of the statutory language that would produce absurd results at odds with manifest Congressional intent."[33] The Commission proposed an application of Section 251(h)(2) that turned on whether a carrier occupied a dominant position in the local exchange market that would make efficient competitive entry difficult "absent compliance with the obligations of Section 251(c)."[34] The ILECs have certainly not shown that an ILEC affiliate providing local service in the same service territory as the ILEC could not meet this criterion. As

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[31] See, e.g., Ameritech Opposition at 10; BellSouth Comments at 9-11.

[32] Declaratory Ruling and Notice of Proposed Rulemaking, Guam Public Utilities Comm'n., 12 FCC Rcd 6925 (1997).

[33] Guam NPRM at ¶ 25.

[34] Id. at ¶ 26.

explained above, such an affiliate, operating in tandem with the ILEC, certainly occupies a dominant position that enables it to make competitive entry more difficult unless it is subject to the obligations of Section 251(c). That is precisely the problem with such affiliates; they allow the ILEC to exploit its dominance, thereby making competitive entry more difficult, by evading the requirements of Section 251(c).

Moreover, such an affiliate could be viewed as having substantially replaced the ILEC, at least with respect to the customers it serves, under Section 251(h)(2)(B), since, like GTA in the Guam NPRM, it "possess[es] all of the advantages of incumbency characteristic of the incumbent LECs described in section 251(h)(1), advantages that can impede the development of competitive markets."[35] Since ILEC affiliates can assist ILECs to exploit the advantages of incumbency to impede the development of competitive markets, they meet the criteria for comparable carriers in Section 251(h)(2), as explicated in the Guam NPRM.

The ILECs also have not presented any obstacle to the treatment of ILEC local service affiliates as dominant, whether or not such affiliates could be deemed ILECs under Section 251(h). The Commission is free to determine whether ILEC affiliates may be treated as dominant, irrespective of their status under the 1996 Act. Ameritech points out that "non-incumbent LECs" are treated as nondominant in the provision of

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[35] Id. at ¶ 33.

access services under the Access Reform Order,[36] but that begs the question of whether ILEC local service affiliates should be treated like ILECs or "non-incumbent LECs" for such purposes of determining dominance.

As to the merits, SNET and GTE argue that ILEC local service affiliates do not have the power to control prices and thus must be considered nondominant.[37] Again, the problem with the ILECs' analyses is that they look at the affiliate in a vacuum, out of context. An ILEC local service affiliate does possess the ability, in tandem with the ILEC, to control prices and to target discriminatory offers. In fact, such an affiliate, unconstrained by Section 251(c), greatly expands the ILEC's ability to control prices on its own. The affiliate's utility in facilitating the ILEC's division and control of the local exchange and access markets in order to frustrate the Section 251 goal of developing local competition requires that such affiliates be treated as dominant.

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[36] Ameritech Opposition at 8 (citing Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers, 12 FCC Rcd 15982 (1997)).

[37] See, e.g., SNET Comments at 8 n. 7.

D. Conclusion

For the reasons stated above and in MCI's initial comments, the relief requested in the CompTel Petition should be granted, and the Commission should issue the requested declaratory ruling and/or initiate the requested rulemaking.

Respectfully submitted,

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